Credit-Related Practices of Islamic Banks in Comparison with Theory: Case Study of Turkey

Z. Hafsa ORHAN ASTRÖM*

Abstract

The aim of this paper is to analyse credit-related practices of Islamic banks in Turkey in comparison with theory. Here, 'credit-related practices' are, first, the bank balance sheet item called 'loans' in general, and second, loans in terms of their types. By 'theory' we mean Islamic economics.

In attaining the aim of this paper, we use comparative methodology depending on quantitative and qualitative research. In this context, we utilize quantitative methods like collecting calculating and representing -through figures and charts- relevant data, and qualitative methods such as searching through, selecting, summarizing and evaluating relevant literature and documents like agreements and reports concerning the subject.

Some of the outstanding results of this paper are as follows; loans are the dominant use of funds for Turkish Islamic banks with changing ratios between 60-75% for the period of December 2005-June 2015 and the main method used for loans is *murabahah* with 99.7% as of June 2015. Secondly, 91% of household loans are in the form of consumer credits as of June 2015, among which house loans are sweepingly dominant. Credits by individual credit cards have been on the increase until the second half of 2013.

Keywords: Islamic banking, credit-related practices, theory, Turkey.

* Ass. Prof. Dr., Istanbul Sabahattin Zaim University, Department of International Trade and Finance, hafsa.astrom@izu.edu.tr
© IJISEF, 2015

Introduction

If Mit Ghamr savings project in Egypt started in 1963 is accepted as the first exemplary application of Islamic banking, then it can be said that Islamic banking has half a century-long history as of yet. Many developments, both in qualitative and quantitative aspects, have taken place during this period. At the point reached today, according to the World Islamic Banking Competitiveness Report 2014-15 (Ernst&Young, 2014), assets of Islamic (participation) banking with commercial banks in core international markets excluding Iran were US$778b in 2013. Furthermore, the industry has gone mainstream in several markets such as Saudi Arabia, Kuwait and Bahrain with more than 48.9%, 44.6% and 27.7% share of markets respectively, and has made considerable progress in a number of emerging markets such as Indonesia, Turkey and Pakistan with 43.5%, 18.7% and 22.0% CAGR (Compound Annual Growth Rate) respectively over 2009-2013 (Ibid.).

At this point, we would like to open a parenthesis for Turkey since it is the country upon which our case study is built. Islamic banks, which started their journey in Turkey in 80s under the name of 'special finance houses', gained the status of 'participation banking' in 2005. This is also why our analysis starts from this date. Including the newly established Ziraat Katilim, currently there are five Islamic banks in Turkey –Kuveyt Turk, Al Baraka Turk, Turkiye Finans and Bank Asya. According to the latest report of Katilim Bankalari (Participation Banking) (TKBB, 2014), total assets of Turkish Islamic banks are 104.1 billion TL while the market share of them is nearly 6%.

In company with developments regarding Islamic finance and banking, there have also been controversial issues such as regulatory issues, standardization and harmonization, Islamic structured products, Islamic capital markets (See: Venardos, 2010). Being one of the controversial issues, credit-related practices of Islamic banks have attracted much interest. First of all, in its broadest meaning, credit-related practices are operations such as loans including *murabahah* (mark-up sale) syndications, funds procured from *sukuk* (Islamic bond) issuance and subordinated loans; financial derivative assets; *ijarah* (leasing transactions); and credit-card issuances. One of the main reasons that the issue is controversial is because these practices are so popular despite harsh critics regarding compatibility of some of them (or the way that they are practiced) with theory. In clarifying what we mean by theory and practice, we can refer to Nagaoka (2012) who openly puts that "Islamic economics is the theoretical background of the practice of Islamic finance".

In connection with all of the above, the aim of this paper is to analyse the credit-related practices of Islamic (participation) banks in Turkey in comparison with theory. What is included in credit-related practices in this paper are; loans/credits as uses of funds and according to their methods used (e.g. *murabahah*, *musharakah* (capital-capital partnership), etc.), and loans specifically given to households under the name of consumer credits and individual credit cards. As remarked by the aforementioned competitiveness report, Turkey is one of the emerging markets in which Islamic banking has made considerable progress. Besides technical conveniences, this fact induces us to analyse Turkey as a case study.

In attaining the aforementioned aim, we use comparative analysis between theory –meaning Islamic economics- and practice which is based on quantitative data and calculations, and qualitative evaluations. Regarding the research steps, for each issue of concern, we first draw a theoretical framework and then make our own analysis regarding facts and figures of particular credit-related activities of Islamic banks in Turkey. Lastly, we compare and discuss the theory and practice of the issues in question.

The difference of our study is that, first, it is about various credit-related activities in depth. Second, it is about Turkish Islamic banks on which studies are rare. Third, we also take into account the difference between theory and practice.

The paper is organized as follows: the following section gives information about relevant literature; second section summarizes the methodology and methods used in this paper; third section is assigned for analysis and evaluation which has two sub-sections, namely 'Loans in General: *Murabahah* vs. Partnership' and 'Loans Given to Households: Consumer Credits and Credit Cards'; the last section concludes the paper.

1. Literature Review

Literature regarding differences between theory and practice of Islamic banking as an institution of Islamic finance draws much interest. Studies discussing the differences between theory and practice of Islamic banking can vary in a wide range. There are, for instance, studies dealing with social issues (See: Zubairu et al., 2011; Asutay, 2012), reasons of the existence of a gap between theory and practice (See: Hasan, 2005; Siddiqi, 2006), and fact and effects of financialisation (See: Tripp, 2006).

Another commonly studied subject in regard to difference between theory and practice is products and operations of Islamic banks. Yousef (2004) calls the dominance of *murabahah* contract, which he describes as akin to the standard debt contract rather than ideal equity contract, in

Islamic banking as '*murabahah* syndrome.' In their study, Samad et al. (2005) first inform that financial contracts such as *mudarabah* (labor-capital partnership), *musharakah*, *qard al-hassan* (benevolent loan) and *istisna'a* (contract of exchange with deferred delivery) are the most distinguished products in theory of Islamic banking. Then, the authors conclude due to their data analysis that in practice, the ratio of the use of these distinguished products is so low for Bank Islam Malaysia (Berhad) and Bahrain Islamic Bank. In another work dealing with difference between theory and practice from the perspective of financial products, Nagaoka (2007) explores the discussions related to *murabahah* and Islamic debt securities which, according to him, have led to divergence in the practice of Islamic finance. In his critical paper, Khan (2010) concludes that the predominance of debt-based/interest-based financing (meaning non-participatory forms such as *murabahah* and *ijarah*) is the norm for Islamic banks. As it can be seen from these works, development and use of more credit/debt-like instruments instead of originally designed or theorized equity-based instruments in Islamic banking is a commonly criticized issue either principally or through empirical studies. It is also possible to find more detailed studies concentrating on one specific operation or product, especially on *murabahah*, due to its position between theory and practice of Islamic banking (See: Cebeci, 2010).

There is also a group of study investigating credit-related activities or operations of Islamic banks without evaluating the subject in terms of the difference between theory and practice. Hatta and Dien (2014) conclude due to empirical facts and figures that debt-oriented Islamic banking products "... have been misleading people through the fractional reserve system towards oft-indebtedness and excessive use of debt for satisfaction and the fulfilment of want for luxuries; that put them and the economy into destructive circumstances." Weill and Godlewski (2012) examine the possible motivations for firms to choose an Islamic loan (provided especially by Islamic banks) over a conventional loan, and identify three country-level determinants in that regard which are religiosity, the share of Muslim population and the quality of institutions and level of financial development. Bendjilali (2000) deals with the issue of demand for consumer credit in an Islamic setting in general, and among others, builds a simple econometric model which can be used to estimate the demand for consumer credit.

On the other hand, the amount of the studies on credit-related activities of Islamic banks in the context of Turkey is not so plentiful. A direct study in that regard is the study of Cokgezen and Kuran (2015) in which they concentrate on the specific issue of Islamic credit cards. The starting point of their paper is the difference between theory and practice since at the very first page, it is written that "One might expect Islamic banks to have ruled out the use of credit cards categorically. After all, their declared purpose is to conduct banking on an interest-free basis." Since the initial assumption of the authors is that charging interest is not harmful, it does not become difficult for them to find supportive evidences through which the difference between conventional and Islamic banking credit cards is shown miniscule. Though it is not only about credit-related activities and Turkey, study of Haron (1998) provides important information about different activities including credit-related ones in Islamic banks in different parts of the world including Turkey. During the time that the article was written, there was only one Islamic bank in Turkey, namely Faisal Finance Institution (FFI). As a credit-related result, Turkish FFI had one of the highest *murabahah* percentages with 61%.

2. Methodology

This paper is, before anything else, a comparative research based on the comparison of theory and practice of outstanding credit-related activities of Turkish Islamic banks. Second, such a comparative research depends on two further well-known methodologies, namely quantitative and qualitative research. In the context of quantitative methodology, we collect, calculate and represent -through figures and charts- relevant data. Meanwhile, in the context of qualitative methodology, we search through, select, summarize and evaluate relevant literature and documents like agreements and reports concerning the subject.

As for research steps based on the aforementioned methodologies and methods, for each credit-related activity, we start by theoretical considerations, then, continue with practical information. Each credit-related activity is ended with a discussion in which comparison of its theory and practice is taken place.

In this paper, necessary data is provided through the Central Bank of Turkey, meanwhile, web sides, contracts of individual Islamic banks, and relevant literature are used for qualitative information. There is also information gathered through personal contacts with some institutions like the Participation Banks Association of Turkey and Kuveyt Turk. For quantitative part, we include four Islamic banks of Turkey into our analysis that are Kuveyt Turk, Albaraka Turk, Turkiye Finans and Bank Asya. The fifth and newly established Islamic bank called Ziraat Katilim is not included due to lack of enough data, as it can be appreciated. For each credit-related item, we make our analysis for the period of December 2005-June 2015, except house and vehicle loans since their data is available from January

2007. Both of these data sets are based on monthly data. Thus, there are 115 entries for the former data set and 102 entries for the latter one.

3. Analysis and Evaluation

In this main section of the paper, we group different credit-related practices of Turkish Islamic banks under two sub-sections, namely 'Loans in General: *Murabahah* vs. Partnership' and 'Loans Given to Households: Consumer Credits and Credit Cards.' Then, for each subsection, we start by theoretical considerations followed by facts and figures. Lastly, we discuss and evaluate the difference between these two.

3.1. Loans in General: *Murabahah* vs. Partnership

Theory

When the idea of Islamic (or interest-free) banking started to take shape, one of the main pillars of it was designed as partnership arrangements instead of interest. In that regard, Qureshi (1945, 2003) condemns *riba* (interest and usury) and suggests profit-and-loss sharing mechanism as an alternative method. According to him, the legal business in Islam is "... co-partnership in which one of the capital supplying partners becomes entitled to the income in view of the capital he supplies without taking any active part in the concern." In a more well-established form of the theory of Islamic banking, Siddiqi (1983, 2006) offers that an Islamic bank might be established on the principle of *shirkat-al-inan* where shareholders own the bank. Furthermore, he indicates that there can be three main activities for the asset side of an Islamic bank; charged services, partnership and *mudarabah* investments, and uncharged services. For the liability side, he mentions *mudarabah* account and loan account. In the end, the early Islamic banks were in fact established based upon the models shaped by early thinkers like Qureshi and Siddiqi.

However, by time, it was understood that partnership arrangements were not enough and suitable for the survival of Islamic banks. Then, a more pragmatic approach was taken which in the end caused among others the introduction of modern version of *murabahah*[1] in late 1970s. Since then, *murabahah* has been the main instrument used by Islamic banks almost all around the world. For studies showing the facts in that regard (See: Rosly, 1999; Samad et al., 2005). Cebeci (2012) explains the reasons of such a phenomenon in detail: First, classical forms of *mudarabah*, *musharakah* and *ijara* were not enough since they could not provide the needs of modern economics. However, modernisation of such instruments (via for example

[1]Compared to its classic version, Guney (2014) describes it as a complex and multi-stage contract. It is also called as 'financing *murabahah*'.

double-tier *mudarabah*) was also not enough to make them alternatives against *murabahah* since people's perspective regarding goods and also their relationship with goods have changed in modern times. People now do not want to have partners against whom they need to be answerable and with whom they would share profits, but they need institutions from where they can loan. Cebeci concludes that besides the factor of people and their understanding of trade, attitude of banks, economic conditions, regulatory factors are also effective in using *murabahah* over idealised partnerships. In this context, there are different studies listing various reasons for dominance of *murabahah* over partnership arrangements such as agency problems, riskiness, lack of property rights for PLS instruments (Dar and Presley, 2000); lack of transparency, high monitoring costs and asymmetric information for PLS instruments (Febianto and Kasri, 2007).

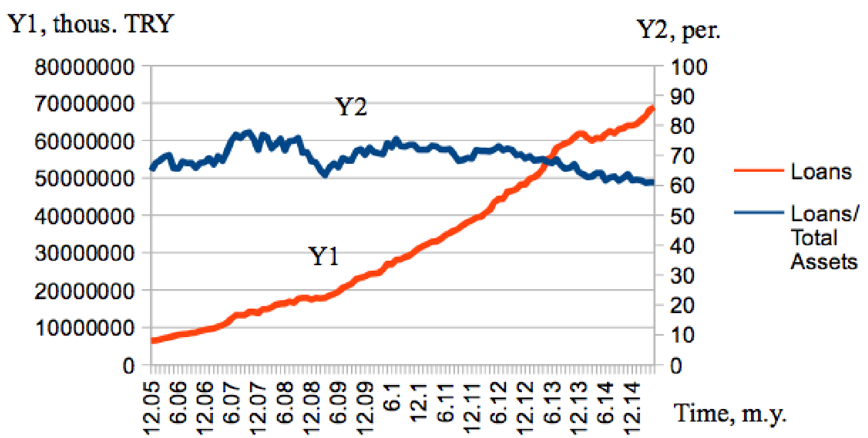
From what is written up until here, it can be argued that *murabahah* was a necessary and useful instrument. Thus, there is no problem in using it instead of originally designed partnership instruments. Insisting otherwise would just be a vain nostalgia. However, the situation is not as simple as it seems. Because, *murabahah* itself is not immune from problems and criticism. Some of them are; having a contract with subject matter different than commodities (such as health care, etc.), shortening the commodity owning period, buy-back arrangement, lack of responsibility of the bank in case that the product is deficient or faulty or seller does not deliver the product to buyer, actualization of 'instalment' agreement between bank and buyer already before the bank buys the product since it reminds the jurisprudential ban of Islam that 'do not sell something that is not with you'. In addition, Bayindir (2005) searches through *murabahah* contracts and notices that some of the Islamic banks include conditions such as payment of interest if there is delay. He says that such conditions put on *murabahah* contracts make Islamic banks credit providing institutions instead of seller of the goods demanded by customers. Guney (2014) lists some of the commonly mentioned problems concerning *murabahah* as the permissibility of unilateral promises to be binding, and avoidance of banks of the risks related to ownership and possession. In a recent study, Amir et al. (2015) criticizes the use of annuities in *murabahah* contract due to its similarity with usury.

Furthermore, as Bacha (1995) points, via use of debt-like instruments such as *murabahah*, Islamic banks will stay in the periphery of the finance and such a case is not compatible with social needs of the countries. Regarding social welfare, Cebeci (2012) concludes that *murabahah*-based Islamic banking promotes individual rather than social *maslahah* (public welfare), and compared to *murabahah*, other instruments like *mudarabah* and *musharakah* seem to be better for expanding welfare and alleviating poverty.

Practice

The question to be asked here is, how is the situation in Turkey in that regard? The relevant item in answering this question is the one shown in Islamic banks' balance sheets as 'loans' (credits). Below graph demonstrates the amount and movement of this item together with its weight in total assets.

Graph 1: Loans, and Loans/Total Assets in Turkish Islamic banks, December 2005-June 2015



Source: Monthly data is taken from the Central Bank of Turkey and graphed by the author.

As it can be seen from Graph 1, loans have increased almost ten times within ten years. After the peak at the end of 2013, there is a relative decrease in the following few months. But, loans have been on an increasing trend since then. When it comes to the weight of loans inside total assets, we see a movement going within the band of 60-75% throughout the period. While the ratio has reached its peak at the end of 2007, it had a sharp decline at the end of 2008 and during the first months of 2009. This can be attributed to global financial crisis. The ratio of loans has been at its lowest levels since last few years, despite that loans are still the dominant item in total assets.

In more detail, according to the information shared by the Participation Banks Association of Turkey[2], 99.7% of loans (meaning almost

[2] This information is gathered through personal contact.

all of the loans) are made to be used via method of *murabahah* while only 0.3% are in form of *musharakah* as of June 2015. This also means that around 60% of funds of Turkish Islamic banks in June 2015 are used via method of *murabahah*.

In order to see in detail how *murabahah* constituting almost all loans is applied by Turkish Islamic banks, we can search through information shared by Islamic banks. Agreements are one of the most direct evidences in this context. Inside the document of 'General Credit/Financing Agreement' (Genel Kredi Sözleşmesi) prepared by Kuveyt Turk[3], the following points come to the fore:

(i) The client cannot demand anything from the participation bank by virtue of fault and confiscation of the good in question, and also of behaviour of the seller. The client irrevocably accepts, declares and promises that all disputes regarding the issue would take place between him/her and the seller (2.2.1).

(ii) Delay Penalty: It defines, in case of delay of payment/default of the client, the amount which needs to be added to delay/default amount after it is calculated with respect to a ratio decided in conformity with reconciliation of the parties, or a ratio determined with regard to this agreement or its enclosures (3.2).

(iii) This agreement is also an irrevocable authorisation and prescription given to the participation bank in determination of the method of payment and its execution. All financial responsibilities concerning payment belong to the client (4.4.).

(iv) (The participation bank) authorises the client for *de facto* receipt of the good subject to financing from the seller (7.1.2).

Firstly, it should be noted here that whether all the items written on contracts are applied or not is another issue needs a separate investigation. However, depending only on contract here, it can be noticed that all these points correspond to controversial aspects of *murabahah* mentioned above. The first and last points imply the lack of responsibility of the bank, whereas, the second point proves the payment of interest (even though it not called with this name) in case of delay. The third point illustrates the permissibility of unilateral promises to be binding, and avoidance of banks of the risks related to ownership and possession.

[3] The contract can be provided upon request.

Additionally, when one clicks and scrolls through the web sites of Turkish Islamic banks, financing options like 'pilgrimage financing', 'education financing', 'health financing' and 'marriage financing' can be seen. In response to our question of how these financings are provided, we are informed by an advisory board member of Kuveyt Turk[4] that such financings are provided through *ijarah* and services financing (meaning *murabahah*). It is added that financing here can also be appraised as *murabahah* of benefit instead of commodity. However, as it was also mentioned above, using *murabahah* for non-material means is another controversial issue.

These facts and figures show that the main use of funding in Turkish Islamic banks is through loans, almost entirely through *murabahah*, with changing ratios between 60 and 75% within the period of December 2005-June 2015. This supports other studies showing dominance of *murabahah* –a debt like instrument in Islamic banking. In fact, in a rare study in terms of *murabahah* usage in Turkish Islamic banks, Haron (1998) informs us that the ratio of *murabahah* in the then solely Turkish Islamic bank, namely Faisal Finance House, was 61%. This number is quite close to the current one. Turkish Islamic banks prefer to use *murabahah* over idealised partnership instruments. Reasons of this choice and how it affects development, social responsibility and genuineness needs a further study.

Additionally, evidences regarding the application of credits in terms of *murabahah* show that there are some issues followed by Turkish Islamic banks which are controversial from the perspective of Islamic jurisprudence.

3.2. Loans Given to Households: Consumer Credits and Credit Cards

Theory

Both the items of consumer credits and credit cards are connected to the issue of consumer behaviour in a wider context. So, we can start our theoretical considerations from there. Since Islamic perspective of life is idiosyncratic, it is expected that people who organize their lives according to this perspective would behave uniquely in different aspects of life such as economics. In his work related to consumer credits from Islamic perspective, Bendjilali (2000) mentions some of the relevant ideas of outstanding Muslim scholars such as Mannan who argues that "taking a loan without any valid reason is discouraged in Islam" and adds that "all types of loans in Islam are to be in nature of grants in aid and not commercial transactions", and Chapra who suggests that "the consumer credit which is considered necessary for realizing Islamic objectives could be arranged by the instalment businesses on a Mudarabah basis". These two names mentioned by Bendjilali

[4] This information is also gathered through personal contact.

are two important figures for the establishment of Islamic economics, meaning theoretical background of Islamic finance institutions.

In a unique work, Khan (2013) attempts to develop an Islamic theory of consumer behaviour based on Islamic theory of economics. In this context, he describes the first element of the framework as relating economic activity of man to the objective of his life. Such a relation necessitates focusing on 'needs' rather than 'utility' as the basis of consumer behaviour. The author describes two categories of needs that are essential and expendable.

In addition, two well-known Islamic consumer behaviour examples concerning credit relations and taking place in hadith literature are that, first, a debtor who has the means of paying his/her debt but delays it oppresses the creditor, and second, if a debtor does not have the means to pay back his/her debt, it is strongly advised that creditor may postpone the payment or even forgive it entirely.

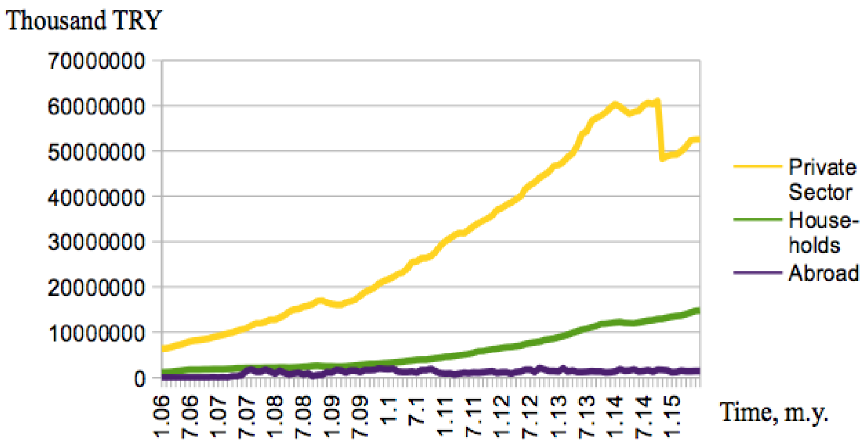
In terms of theoretical considerations regarding credit cards, Aktepe (2010) informs us that their evaluation from the perspective of Islamic jurisprudence has been on agenda since last 20 years. He underlines that commission taken from card holders by Islamic banks is especially controversial. He also mentions new proposals like *murabahah* card and strong oppositions against it. Bayindir (2005) gives credit cards a considerable amount of place in his work. After explaining that legal relationship between bank, card holder and member place of business should be accepted as the sum of agreements of guaranty (*kafalah*), transfer (*hawala*) and service, he clarifies why commission taken from the place of business by bank is legitimate. On the other hand, he explains, when a card holder uses his/her credit card in order to get cash, there are two options: either he/she withdraws his/her own money from his/her account or receives debt because of the option of credit. Discussions start within the context of the second one since legal situation and thus legitimacy of commission becomes problematic here. But there is a general agreement on its legitimacy if the commission in question is the same for all types of debt and depending only on service and cost. Having said that, there is also unanimity on unlawfulness of any of the following surpluses taken from debt which is based on debt relationship between card holder and bank: interest and cash advance commission taken from cash credit, limit exceeding fee taken when card holder exceeds credit limit while buying something or withdrawing cash, credit interest taken if card holder wants to pay some parts of his/her expenses by instalment, and interest for late payment taken if the minimum amount of debt which arises due to cash withdrawal or purchase of something is not paid on time. Bayındır summarizes that Islamic banks started to provide credit cards because of meeting credit card demands of their customers and also utilizing commission revenue from member places of business. However, since surplus taken in result of instalment of debt becomes interest, Islamic banks could not apply it. When they do instalment without any charge, they lose money due to inflation, thus Islamic banks have applied it via taking into account inflation. Now Islamic banks want also bring-in from card holders while card holders want that their debts are installed. This brings new and different suggestions forward such as instalment card and *murabahah* card. As Aktepe, Bayindir discusses reactions against especially the second one which is approved by scholars like H. Karaman.

Inside the report prepared in result of the consultation meeting about contemporary religious issues (Presidency of Religious Affairs, 2013), issues regarding Islamic credit cards that need to be questioned are listed as follows: 1. Marketing morality should be examined carefully since there should not be any encouragement for heavy consumption 2. Islamic banks should be aware of the habits and choice of place of business of their customers in order to see whether they match with their profile. 3. Card holders should be informed that they need to pay a compensation under the name of interest in case of delay.

Practice

Now, in terms of the practice regarding consumer credits and credit cards, we can first search through details of loans shown on Graph 1 in terms their types. The top three items and their movements throughout the period of December 2005- June 2015 can be seen from the following graph:

Graph 2: Loans given by Islamic banks in Turkey in terms of their types, December 2005-June 2015.

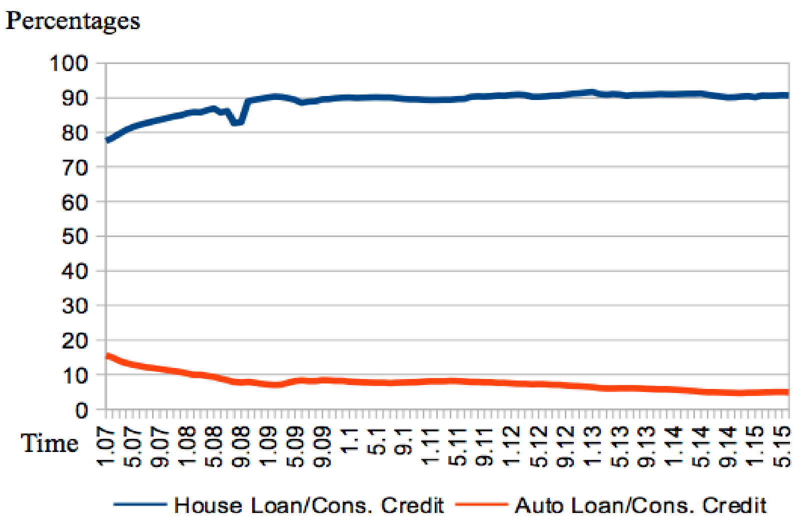


Source: Monthly data is taken from the Central Bank of Turkey and graphed by the author.

It can be seen that loans are especially provided for private sector (76% of loans as of June 2015) and households (21% of loans as of June 2015). These two are followed by loans taken by abroad. While there is a more stable increase in loans taken by households, private sector loans are relatively more volatile, especially with a sharp decline at the end of 2014.

Here, we will especially deal with loans given to households. In practice, the main element of loans given by Turkish Islamic banks to households is 'consumer credits'. The ratio of consumer credits to loans given to households has been within the band of 73-91% in period of December 2005-June 2015. The important point here is that there is an increasing trend since the end of 2013 and the ratio in question is 91% as of June 2015. When content of consumer credits is searched in detail, it can be seen that the two outstanding elements are house and automobile loans. As a small note here, the last item under consumer credits, meaning 'credits for needs and other credits', has been around 4-6% throughout the period of January 2007-June 2015. On Graph 3, one can see the movements of the weight of house and automobile loans with respect to consumer credits throughout the period of January 2007-June 2015.

Graph 3: Ratios of house and automobile loans to consumer credits given by Turkish Islamic banks, January 2007-June 2015



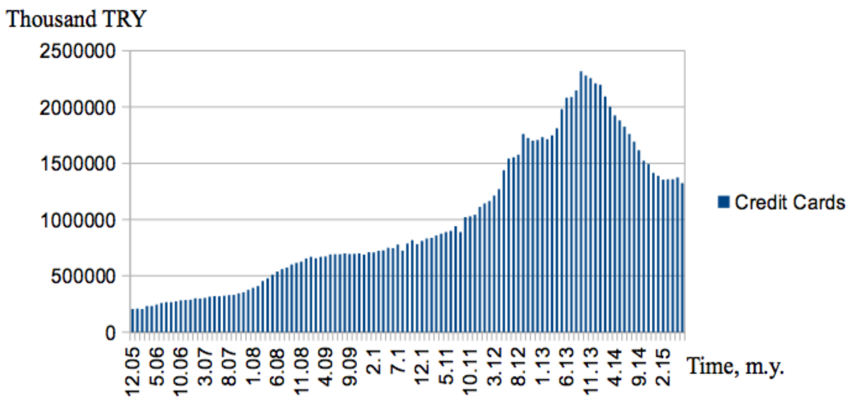
Source: Monthly data is gathered from the Central Bank of Turkey and graphed by the author.

A great difference between house loans and automobile loans with respect to consumer credits, because, while the weight of house loans in consumer credits has been around 90% since few years back, the highest ratio of auto loans to consumer credits was 15.56%, and this was in 2007. It can also be seen that while there is not a long period of decrease in house loans with respect to consumer credits (except a short period at the end of 2008 due to financial crisis), the weight of automobile loans in consumer credits has been almost in a constant decrease since the middle of 2011.

In order for comparison, for conventional banks, credits to households include consumer credits, individual credit cards and credits given to personnel. Inside the item of consumer credits, there are credits of house, vehicle, needs and others. Consumer credits in Turkish conventional banks (again according to data of the Central Bank of Turkey) have been moving in the band of 62-80% with a relatively constant increase from December 2005 till 2015. It can be noticed that, this band is having higher ends (73-91%) for Islamic banks. Furthermore, while the ratio of house loans to consumer credits for Turkish conventional banks has been inside the band of 40-50%, the ratio of vehicle loans to consumer credits almost constantly decreased from 22% to 2% during the same period. These trends seem similar with Islamic banks despite Islamic banks still have higher ratios of house and automobile/vehicle loans. In contrast to Islamic banks, however, ratio of 'credits for needs and other credits' with respect to consumer credits in conventional banks was around 35% as of December 2005 and became 54% as of June 2015.

'Credit cards' is another item under the heading of loans given to households besides consumer credits. Amount of credits reached by credit cards and its movement can be seen from the following graph:

Graph 4: Amount of credits reached by Islamic credit cards, December 2005-June 2015.



Source: Monthly data is gathered from the Central Bank of Turkey and graphed by the author.

As it can be seen from Graph 4, there is an increasing trend in amount of credits reached by credit cards until the end of 2013 where they also have reached their peak. Then there is a sharp decline till the end of 2014. On the other hand, the ratio of credits of credit cards to household loans decreased from 18% to 9% throughout the period. Again in terms of comparison, ratio of credits of credit cards provided by Turkish conventional banks with respect to household loans decreased from 37% to 20% within the period of December 2005-June 2015.

According to information shared by Cokgezen and Kuran (2015), Ihlas Finance was the first credit card issuer as a special finance house in Turkey in 1986 while Bank Asya issued the first *bona fide* card in 2002. Currently, Islamic banks are owning around 3% of entire card market in Turkey.

Details of the application of Islamic credit cards can be followed from relevant documents and agreements. Inside the agreement for general credits prepared by Kuveyt Turk, the following points related to credit cards come to the fore:

(i) Customer/additional card holder can withdraw cash via using the card code from his/her balance if his/her account is suitable. Furthermore, customer/additional card holder can withdraw cash advance within the limit of cash advance allocated by the Participation Bank… if there is an expense more than his/her existing balance or limit, then this extra amount should immediately be given back to the Participation Bank, otherwise, a delay penalty would be applied since the day of the transaction (14.3.2.2.).

(ii) Participation bank has the right to determine the transaction fee, commission and other amounts that the bank would register as debt for the account of the customer in result of cash advance withdrawals (14.3.2.4).

(iii) When customer demands instalment of total expenditure, this amount would be installed by means of inclusion of profit sharing ratios applied by Participation Bank on date of transaction (14.3.3.2).

It can be realized that the first point is related to two options mentioned by Bayindir in getting cash. Here, a delay penalty is applied if the extra amount is not immediately paid back. This seems like limit exceeding fee listed as one of the illegal commissions. The second point is related to cash advance withdrawals. As explained by Bayindir, cash advance withdrawal commission is a regular fee commission if it is done directly from the account, and if it is in terms of cash credit, it is acceptable under the condition that it is fixed and not changing according to debt types and amounts. Here, we cannot find any particular mentioning of such an arrangement. The explanation regarding commission is rather vague. The third point clearly explains the use of instalment option with profit sharing ratios, not with inflation-based ratios.

According to a report prepared by Kaya (2009) Point 26 of the Law Concerning Bank Cards and Credit Cards in Turkey, which is related to calculation of interest, informs that if some parts of debt is paid, interest is calculated for the rest of the balance of account. If the paid amount was exactly as or higher than the minimum amount of payment, contractual interest, and if a less than minimum amount is paid, then interest for delay is calculated for the rest of the balance of account. As for participation banks, contractual interest is applied according to profit sharing ratio while interest for delay is applied as delay penalty. When theoretical considerations are taken into account, it does not seem appropriate for Islamic banks to take anything for the first case because it would be as if taking interest for debt instalment, and also for the second case since it would be as if taking interest for late payment. Calling it 'profit sharing ratio' would not change the situation.

In a rare study concerning the application of Islamic cards in Turkey, Cokgezen and Kuran (2015) first give some imaginary examples in order to show how Islamic cards are applied in Turkey. In their first example, a card holder pays the minimum amount of his/her debt but wants to pay the rest later on. However, then, the customer would be charged because of late payment. The authors give this example as a commission on late payment but, given the aforementioned Point 26, it actually seems an example of instalment of debt which conventional banks take contractual interest from and which is not acceptable from Islamic perspective whether it is applied by Turkish Islamic banks or not. Even if this was the example of commission on late payment, it is obvious that this is not allowed in Islamic jurisprudence. In their second example, it seems that they are questioning service commission taken from customers. Discussions regarding it and conditions under which such an application would be acceptable was explained by Bayindir above. In third example, commission taken from cash credit under the name of time-dependent charge (or inflation-based charge) is mentioned. Bayindir also explains this above. Then the authors touch upon the issue whether consumption of card holder is really Islamic. This point was underlined together with a solution suggestion by the Presidency of Religious Affairs (PRA) above. The authors also mention the application of *murabahah* card but, whether it is applied or not, there are serious critics against it. As other controversial issues, they mention the use of liquid assets by credit cards and consumption effect of credit cards –like bonus applications. Consumption effect of credit cards were also underlined by PRA before.

In terms of evaluation, firstly, less than a quarter of loans/credits of Turkish Islamic banks are given to households. Yet both in terms of amounts, and ratios with respect to loans in general, household loans have been increasing since especially the middle of 2010. Consumer credits are quite high among household loans and they are still increasing. Inside consumer credits, there is an accumulation around house loans. In comparison with theory, loans are especially organized as *murabahah* instead of e.g. 'instalment on *mudarabah* basis'. On the other hand, getting loan for valid reasons or for necessity does not seem entirely lacking since loans for house –which is one of the main necessities of today's human being- are so high. However, since Islamic banks are commercial institutions, grants that are not in commercial transactions are yet to be developed.

In comparison with conventional banks, despite the existence of a similar movement, consumer credits take larger (around 10% more) portion inside household loans. Again, though the movements of house loans within consumer credits are similar, ratio of house loans to consumer credits for

Turkish Islamic banks is higher than conventional banks' house loans. Difference this time is bigger, meaning 20-30%. The ratios of vehicle loans to consumer credits have both more similar numbers and movements between Islamic and conventional banks. The main difference between these two types of banks regarding consumer credits is the high ratio of 'credits for needs and other credits' in conventional banks. This makes sense since Islamic banks are not supposed to be credit providing institutions, especially if the matter of credit is a non-material thing.

History of Islamic credit cards is not so old in Turkey. Even though increase in use of Islamic credits cards is not as tremendous as in Malaysia (See: Idris, 2012), if suggestions like *murabahah* card is fully put into practice, then situation can change. However, a more concern should be on legal arrangements regarding Islamic credit cards and validity of these arrangements from Islamic perspective. Special concern is needed for issues like the extra amount taken from cash credit, limit exceeding fee taken when card holder exceeds credit limit while buying something or withdrawing cash, an extra amount taken if a card holder wants to pay some parts of his/her expenses by instalment, and an extra amount for late payment taken if the minimum amount of debt arises due to cash withdrawal or buying something is not paid on time. Another important issue in that regard is consumption effect of Islamic credit cards in Turkey. However, this important subject necessitates a separate study.

Conclusion

In this paper, we analysed the following credit-related practices of four Turkish Islamic banks for the period of December 2005-June 2015; loans in general and in terms of methods used (such as *murabahah*, etc.), and loans in terms of their types. Such an analysis was conducted by collecting, calculating and presenting relevant data gathered from the Central Bank of Turkey. Then, results of our analysis were compared with theoretical framework –searched, selected, evaluated and given place by us in separate sub-sections- drawn inside the boundary of Islamic economics.

As one of the results of this paper, the main use of funds of Turkish Islamic banks is through loans (between 60-75% for the period of December 2005-June 2015) and almost all of these loans (99.7% as of June 2015) are using the method of *murabahah*. Besides theoretical concerns regarding negative effects of using *murabahah*, there are some jurisprudential concerns in their application such as the lack of responsibility of the bank, the payment of interest (even though it is not called with this name) in case of delay, the permissibility of unilateral promises to be binding, avoidance of banks from risks related to ownership and possession, and using *murabahah* for non-material means.

As for loans in terms of their types, nearly a quarter of loans are given to households. Inside household loans, consumer credits are leading (with 92% as of June 2015), whereas credits by individual credit cards are also substantial. On the other hand, consumer credits are especially given for house loans (95% as of June 2015). In comparison with theory, it can be seen that loans are organized as *murabahah* instead of idealised partnerships such as *musharakah*. As an important element of Islamic consumer behaviour, getting loan for valid reasons or for necessity does not seem entirely lacking because of the dominance of loans for house –which is one of the main necessities of today's human being. However, grants that are not in commercial transactions are yet to be developed, if ever it can be.

Even though Islamic credit cards are not in extreme amounts in Turkey (4-5% of entire credit market) as in some countries like Malaysia, more attention should be given to some jurisprudential issues like extra amount taken from cash credit, limit exceeding fee taken when card holder exceeds credit limit while buying something or withdrawing cash, an extra amount taken if a card holder wants to pay some parts of his/her expenses by instalment, and an extra amount for late payment taken if the minimum amount of debt arises due to cash withdrawal or buying something is not paid on time. Another important issue to be taken into account is the consumption effect of Islamic credit cards in Turkey.

At the end, we should add that this paper uses mostly contract information while evaluating the practices of Islamic banks. A more detailed investigation in applications of them can be another research project.

References

Aktepe, Emin, Ishak (2010), "Kredi Karti Sistemi ve Islam Hukuku Acisindan Degerlendirilmesi", *Dinbilimleri Akademik Arstirma Dergisi*, Cilt 10, Sayi 1, ss. 133-1.

Amir, Vaisal; Hatimah, Husnul; Khalisah, Nur, and Purboyanti, Rini, Trah (2015), "A Criticism of Annuities in Murabahah Transaction: Allowing Riba Through Fatwa?", Proceeding-Kuala Lumpur International Business, Economics and Law Conference 6, Vol. 1, April 18-19, 2015, Hotel Putra, Kuala Lumpur.

Asutay, Mehmet (2012), "Conceptualising and Locating the Social Failure of Islamic Finance: Aspirations of Islamic Moral Economy vs. Realities of Islamic Finance", *Asian and African Area Studies*, Vol.11, No. 2, pp. 93-113.

Bacha, Obiyathulla, Ismath (1995), "Conventional versus Mudarabah Financing: An Agency Cost Perspective", *Journal of Islamic Economics*, No. 4, No. 1-2, pp. 33–49.

Bayindir, Servet (2005), *Islam Hukuku Penceresinden Faizsiz Bankacilik*, Ragbet Yay., Istanbul, Turkey.

Bendjilali, Boualem (2000), *On the Demand for Consumer Credit: An Islamic Setting*, Islamic development Bank, Research Paper 30, Second Edition, Jeddah.

Cebeci, İsmail (2012), Integrating the Social Maslaha into Islamic Finance, *Accounting Research Journal*, Vol. 25, Issue 3, pp. 166-184.

Cebeci, İsmail (2010), *Modern İslam İktisadı Literatüründe Murabaha Tartışmaları*, Yayinlanmamis Doktora Tezi, Marmara Universitesi Sosyal Bilimler Enstitusu, Istanbul.

Cokgezen, Murat, and Kuran, Timur (2015), *Between Consumer Demand and Islamic Law: The Evolution of Islamic Credit Cards in Turkey*, ERID (Economic research Initiatives at Duke) Working Paper 182, Duke.

Dar, Humayon, A., and Presley, John, R. (2000), "Lack of Profit-Loss Sharing in Islamic Banking: Management and Control Imbalances", *International Journal of Islamic Financial Services*, Vol. 2, No. 2, pp. 3-18.

Ernst&Young, (2014), *World Islamic Banking Competitiveness Report 2014-15: Participation Banking 2.0*.

Febianto, Irawan, and Kasri, R. A. (2007), "Why Do Islamic Banks Tend to Avoid Profit and Loss Sharing Arrangements?", 2nd Islamic Economics Conference, Islamic Science University of Malaysia, Kuala Lumpur.

Guney, Necmeddin (2014), "Murabaha Financing Revisited: The Contemporary Debate on Its Use in Islamic Banks", 5th International Conference on Islamic Jurisprudence in the 21st Century, Department of Fıqh and Ulul al-Fıqh, International Islamic University of Malaysia, Kuala Lumpur.

Haron, Sudin (1998), "A Comparative Study of Islamic Banking Practices", *J. KAU: Islamic Econ.*, Vol. 10, pp. 23-50.

Hasan, Zubair (2005), "Islamic Banking at the Crossroads: Theory versus Practice", *Islamic Perspectives on Wealth Creation*, Ed.: Munawar

Iqbal and Rodney Wilson, Edinburgh University Pres., Edinburgh, UK.

Hatta, Mohammad, Firdaus, Mohammad, and Dien, Mawil, Izzi (2014), "Examining the Dominance of Islamic Debt-based Products in the Economy", *International Journal of Arts and Commerce*, Vol. 3, No. 6, pp. 13-28.

Idris, Umar, Mohammed (2012), "Effects of Islamic Credit Cards on Customer Spending", International Trade&Academic Research Conference (ITARC), 7-8th November, London.

Kaya, Ferudun (2009), *Turkiye'de Kredi Karti Uygulamasi*, Turkiye Bankalar Birligi (Banks Association of Turkey), No. 263, Istanbul.

Khan, Fahim (2010), "How 'Islamic' is Islamic banking?", *Journal of Economic Behavior&Organization*, Volume 76, Issue 3, pp. 805-820.

Khan, Fahim (2013), "An Alternative Approach to Analysis of Consumer Behaviour: Need for Distinctive "Islamic" Theory", *Journal of Islamic Business and Management*, Vol. 3, No. 2, pp. 1-35.

Nagaoka, Shinsuke (2012), "Critical Overview of the History of Islamic Economics: Formation, Transformation, and New Horizons", *Asian and African Area Studies*, Vol. 11, Number 2, pp. 114-136.

Nagaoka, Shinsuke (2007), "Beyond the Theoretical Dichotomy in Islamic Finance: Analytical Reflections on Murabahah Contracts and Islamic Debt Securities", *Kyoto Bulletin of Islamic Area Studies*, 1-2, pp. 72-91.

Presidency of Religious Affairs, (2013), *Güncel Dini Meseleler Istisare Toplantisi-III*, 10-12 Aralik, Afyonkarahisar.

Qureshi, Anwar, Iqbal (1945, 2003), *Islam and the Theory of Interest*, Kitab Bhavan, New Typesetting, New Delhi, India.

Rosly, Saiful, Azhar (1999), "'Al-Bay' Bithaman Ajil Financing: Impacts on Islamic Banking Performance", *Thunderbird International Business Review*, Vol. 41, Issue 4-5, pp. 461-80.

Samad, Abdus; Gardner, Norman, D., and Cook, Bradley, J. (2005), "Islamic banking and finance in theory and practice: The experience of Malaysia and Bahrain", *The American Journal of Islamic Social Science*, Vol. 22, No. 2, pp. 69–86.

Siddiqi, Muhammad, Nejatullah (2006), "Islamic Banking and Finance in Theory and Practice: A Survey of the State of the Art", *Islamic Economic Studies*, Vol. 13, No. 2, pp: 2-48.

Siddiqi, Muhammed, Nejatullah (1983, 2006), *Banking Without Interest*, The Islamic Foundation, Reprinted, Leicestershire, UK.

TKBB (Participation Banks Association of Turkey), (2014), *Katilim Bankalari 2014*, TKBB, Istanbul.

Tripp, Charles (2006), *Islam and the Moral Economy: The Challenge of Capitalism*, Cambridge University Press, Cambridge, UK.

Venardos, A. M. (2010) (*ed.*), *Current Issues in Islamic Banking and Finance: Resilience and Stability in the Present System*, World Scientific Publishing Co. Pte. Ltd., Singapore.

Weill, Laurent, and Godlewski, Christophe (2012), *Why do large firms go for Islamic loans?*, BOFIT (Bank of Finland, Institute for Economies in Transition) Discussion Papers 7, Helsinki.

Yousef, Tarik, M. (2004), "The Murabaha syndrome in Islamic finance: Laws, institutions and politics", *The Politics of Islamic Finance*, Ed.: Clement Henry and Rodney Wilson, Edinburgh University Press Ltd, Edinburgh, UK.

Zubairu, Umaru, Mustapha; Sakariyau, Olalekan, Busra, and Dauda, Chetubo, Kuta (2011), "Social Reporting of Islamic Banks in Saudi Arabia", *International Journal of Business and Social Science*, Vol. 2, No. 23, Special Issue, pp. 193-205.